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value for all customers

Direct Dial: 020-7901-7355

5 October 2006

Electricity Distributors, Electricity Suppliers,
Distributed Generators and Interested Parties.

Dear Colleague,

Designation of the Distribution Connection and Use of System Agreement (DCUSA).

1. On 29 August 2006 Ofgem¹ issued a notice of our intention to designate the DCUSA². That notice invited comments on both our intention to designate the DCUSA and its contents. On 29 September 2006, we issued a notice of our decision to designate the DCUSA and directed that changes between the consolidated agreement for use of system (consolidated DUoSA) and the DCUSA be made³. The reasons for this direction are provided in this letter.
2. In making our decision, we have had regard to whether the DCUSA meets the requirements of Standard Licence Condition 9B of the Distribution Licence. We have also had regard to whether it would be in accordance with Ofgem's principal objective and general duties to make this decision, and have considered the representations made in response to the notice of our intention to designate the DCUSA. A separate letter, issued on the same date as this document, provides the formal legal designation. That letter can be seen by clicking [here](#).

Background

3. The governance arrangements for electricity distribution have been under review since April 2002. Ofgem's document *Governance in the electricity Distribution Commercial arrangements: Conclusions and Final Proposals*⁴ (the Conclusions Document) set out the following reasons as to why change is desirable:
 - the development of the DCUSA would create greater transparency by centralising information relating to connection to and use of the distribution networks;

¹ The terms 'the Authority', 'Ofgem' and 'we' are used interchangeably in this document. Ofgem is the Office of the Gas and Electricity Markets Authority.

²http://www.ofgem.gov.uk/temp/ofgem/cache/cmsattach/16722_DCUSA_Notice.pdf?wtfrom=/ofgem/work/index.jsp§ion=/areasofwork/elecgov/egov04

³http://www.ofgem.gov.uk/temp/ofgem/cache/cmsattach/14570_6506.pdf?wtfrom=/ofgem/work/index.jsp§ion=/areasofwork/elecgov/egov04

⁴http://www.ofgem.gov.uk/temp/ofgem/cache/cmsattach/12932_Gov_in_Elec_Dist_Comm_Arrs_Ofgem_Conclusions.pdf?wtfrom=/ofgem/work/index.jsp§ion=/areasofwork/elecgov/egov04

- replacing approximately 400 bilateral contracts with a single standardised document would benefit competition by enabling new entrants to come to the market without having to negotiate bespoke contracts;
 - flexible governance may better enable industry to adapt the Code to meet future changes and developments in industry; and
 - those changes would take place in a more transparent and consistent way, thus facilitating principles of good governance and competition.
4. In line with the recommendations in the Conclusions Document, on 5 April 2006 Ofgem issued a Collective Licence Modification introducing Condition 9B. This placed an obligation on electricity distributors to develop the DCUSA in accordance with the requirements of the condition. A steering group (the DCUSA Steering Group) was created, to prepare the DCUSA and discharge this obligation. Condition 9B also required that, subject to the Authority designating the DCUSA, industry participants holding Electricity Distribution Licences must accede to the DCUSA, maintain it, and comply with it. A similar condition was inserted into the Electricity Supply Licence requiring, amongst other things, suppliers to be a party to the DCUSA from the date of designation and comply with it.
 5. Condition 9B states that prior to designating the DCUSA Ofgem must give notice of its intention to do so and set out the contents of the proposed DCUSA to enable interested parties to comment on that document. On 29 August 2006 Ofgem issued such a notice and invited comments on the draft DCUSA on or before 26 September 2006. The responses to that consultation have been received and taken into account by Ofgem in its decision to designate the DCUSA. The responses can be found, in full, on the Ofgem website.

Industry Responses to Notice of Intention to Designate

6. On the whole, the responses received were in favour of designation of the DCUSA. Whilst this is the case, the responses received during the consultation period highlighted issues over which parties had concerns. These are addressed in the following paragraphs.

Revenue Protection

Respondents' views

7. One respondent expressed a strong preference for the insertion of an obligation requiring suppliers to accept the revenue protection services from a particular network operator. The party considered that this would be appropriate on the basis that it would be in the interests of customers. The respondent commented that in its view, the drafting of the DCUSA in relation to this issue was changed too late in the day, and that insufficient thought had been given to an alternative framework to support revenue protection services. The respondent considered that designation should not take place until such issues had been resolved satisfactorily. It also cited a lack of progress in relation to minimising levels of energy theft over recent years and suggested that no changes should be made to the delivery of revenue protection services until it is established that a better solution is possible.
8. The respondent also sought to rebut the reasons previously cited by Ofgem as to why a clause enabling a particular party to require its users to accept revenue protection services would not be appropriate. One of Ofgem's reasons was that such a change would introduce a regional variation. The respondent commented

that although this was the case, Condition 9B requires the DCUSA to cover revenue protection and to be consistent with the efficient distribution of electricity. Another Ofgem statement commented on by the respondent was that the DCUSA should not mandate services for which revenues are excluded from the price control. The respondent considered that it had always been accepted that one of the reasons for excluding revenues from price control was because the transaction volumes were uncertain.

9. A counter view held by one supplier respondent was that the clause in question should remain unchanged as revenue protection services should be provided at the request of the supplier and it should not be mandatory for suppliers to take this as part of a use of system service agreement.
10. Another respondent stressed its concern that the revenue protection clause in the DCUSA gives suppliers the option to obtain such services elsewhere despite Ofgem's review of revenue protection not having concluded. The user expressed concern about its ability to offer a comprehensive service to the benefit of all consumers being undermined.
11. Another point raised during consultation was that revenue protection should be a part one matter and so only amenable to amendment with the approval of the Authority.

Ofgem's view

12. Ofgem considers the provision of revenue protection services an important one that has the potential to impact on customers' costs. We acknowledge that important issues related to revenue protection are yet to be resolved by industry and that these are being addressed in the work being taken forward by industry groups. These industry groups have indicated they will be in a position to reach their conclusions on this issue and make recommendations to Ofgem by the end of 2006.
13. It may be that the DCUSA will provide a vehicle to implement the recommendations. Nevertheless, this would not preclude parties from raising change proposals to address revenue protection issues at any time after designation of the DCUSA.
14. In any case, Ofgem considers that it would be more appropriate for terms relating to revenue protection services to exist on a multi-lateral rather than a bi-lateral basis. Ofgem notes that Condition 9B requires the DCUSA to be consistent with the efficient distribution of electricity. However, Ofgem is not convinced that the drafting preferred by the respondent would be consistent with the efficient distribution of electricity. Ofgem is also concerned that any solution should not work to the detriment of the general regulatory framework because Ofgem considers it would be inappropriate for Suppliers to be under an obligation to take revenue protection services while these services are excluded from the price control.
15. Nevertheless, there is a licence obligation on Suppliers to take all reasonable steps to detect and prevent theft and to inform distributors. We expect Suppliers to take this obligation seriously.
16. In response to the second respondent's concern about the long term impact of the ability of suppliers to obtain revenue protection services elsewhere, Ofgem notes

again that there is no industry consensus on the issue of revenue protection. As mentioned above, the subject is currently under review.

17. In relation to revenue protection being a part one matter, Ofgem considers that the terms as presently drafted in relation to revenue protection are more appropriate to sit in part two of DCUSA. This is because Ofgem does not consider that the absence of an obligation on Distribution Network Operators (DNO) to provide, and a corresponding obligation for suppliers to take revenue protection services, would in itself have a direct and significant impact on customers, sufficient to warrant inclusion into part one of the DCUSA. However, Ofgem notes that in the event that a change proposal was put forward to amend these or new revenue protection terms and it was Ofgem's view based on the detail and impact of the specific proposal that it should be treated as a part one matter in accordance with the DCUSA criteria (clause 9.4), Ofgem could require such a proposal be treated as a part one change proposal and therefore subject to Authority approval.
18. In conclusion, Ofgem considers revenue protection an important issue and one that needs to be addressed coherently and consistently for the long term benefit of customers. The industry review is progressing and there will be an opportunity to implement a comprehensive change on its conclusion. Notwithstanding this, given the opportunity at any stage for change proposals to be raised, there is not sufficient justification against the overall benefits of the DCUSA to warrant a delay in its designation.

Sharing the Market Domain ID

Respondents' views

19. It was suggested that it would be inappropriate to introduce the concept of a shared Market Domain ID as such a concept does not feature in the existing DUoSA and would also be in conflict with other existing industry documents.

Ofgem's view

20. Ofgem understands that the concept of shared Market Domain IDs exists in practice in a limited number of instances, although the concept was not carried over into the consolidated DUoSA. During preparation of the DCUSA, Steering Group parties undertook an assessment of this aspect of the agreement. On the basis of that assessment, the majority of industry agreed to formalise the concept of a shared Market Domain ID in the DCUSA. Ofgem notes that the concept is different to arrangements under the BSC and the MRA but does not conflict with those documents. At present, Ofgem sees benefit in having single IDs in terms of the efficiency of the arrangements, but nevertheless has directed this change. These reasons are given below in the section headed *Direction of differences between consolidated DUoSA and DCUSA*.

Credit Cover

Respondents' views

21. One respondent believed that a common interpretation of VAR and payment record is not likely to be reached in the short term. In view of this it was suggested that it would be appropriate to put in place a 6 month derogation from the requirement to bring these aspects of the credit cover arrangements into effect.

Ofgem's view

22. We consider that the credit cover arrangements as set out in the DCUSA represent an improvement on the previous credit cover arrangements. Ofgem does not consider that complete agreement between parties on all the terms of the Agreement is a pre-requisite prior to designation. We note that parties will be able to bring forward change proposals to refine the DCUSA where appropriate.
23. Regarding a request for a derogation, Ofgem's view is that parties have been aware of the shape of the credit arrangements during the development of the consolidated DUoSA and more recently during the development of the DCUSA. Parties have been aware of the likely impact of the document and have had time to make necessary preparation. In August 2006, Ofgem stated its intention to designate the DCUSA on the terms detailed. We consider that it would not have been unreasonable for parties to make preparatory steps to facilitate compliance should a decision be made to Go-Live in October 2006.

Ofgem's role in the assessment process

Respondents' views

24. One respondent suggested that the addition of a clause to allow Ofgem to allocate a part two change proposal to part one (where Ofgem considers the proposal meets the DCUSA criteria) has increased Ofgem's regulatory powers to intervene in decisions made by the industry. It was suggested that this clause increases regulatory uncertainty and provides Ofgem with extended powers to intervene which do not currently exist. The respondent considered that this is not in line with the principle of rolling back regulation where ever possible, and runs counter to the present DTI initiative to reduce the regulatory burden across markets. It was also suggested that this arrangement will have the effect of removing the distinction between part one and part two of the DCUSA as ultimately all changes will be determined by Ofgem. The respondent stressed that it accepted it is not Ofgem's intention to undermine the processes or the operation of the Panel, but believed that this will ultimately be the effect of this new clause. It was suggested that a better approach to this issue would have been to rely on the provisions which allow the Consumer Council to attend Panel meetings and propose changes to the agreement.
25. A counter view from one respondent was that they do not believe that the Authority's principal objective to protect the interest of consumers can be diluted or legislated away under the DCUSA by the determination of the Panel and that the final draft text of the DCUSA which contains provisions for the Authority to review the Panel's allocation of change proposals into part two is appropriate.

Ofgem's view

26. To designate DCUSA in the absence of an adequate safeguard against inappropriate allocation of proposals into part two by the DCUSA Panel could compromise our principal objective and general duties, particularly to protect the interests of consumers. Our assessment is that these arrangements strike the right balance between 'light touch' regulation and the protection of consumers' interests. We therefore consider that the provisions of clause 11.21 are appropriate.

Ofgem's decision not to undertake another Impact Assessment

Respondents' views

27. One respondent suggested that Ofgem should undertake another Impact Assessment on the basis that, for resource constrained organisations, the consultation issued on 29 August 2006 represents the only opportunity to comment on the final draft. Another respondent suggested that it would be appropriate to undertake another Impact Assessment at this point on the basis that the document as currently drafted poses the risk of a vacuum being created in which important services are not adequately provided for. It was suggested that these risks would be picked up if Ofgem were to conduct an Impact Assessment focussing on the changes in the commercial terms rather than on the governance arrangements. The respondent highlighted its particular concern over the impact which the alterations of the clause relating to revenue protection would have on consumers.

Ofgem's view

28. The DCUSA process has been under development for over three years. It has been subject to extensive consultation and detailed discussion in working groups. In May 2005 a full Impact Assessment was published. A decision document was developed in response and the detailed DCUSA developed by an industry steering group. In the light of the extent of consultation and involvement across the sector, Ofgem considers it would be disproportionate to undertake another Impact Assessment.

DNO voting arrangements

Respondents' views

29. One respondent suggested that it was inappropriate to institute different voting arrangements for Distribution Network Operators as compared to those used for other classes of party. The respondent was concerned about the voting power available to integrated companies with supply and distribution interests, and was reluctant to see the position of stand-alone distributors further weakened by the removal of the party-group concept.

Ofgem's view

30. In our Conclusions Document we recommended that a safeguard such as that referred to by the respondent would be an appropriate feature. However, notwithstanding this, we do not judge that this issue is sufficient to justify delaying the designation of the DCUSA given the clear benefits which can be gained consistent with the licence requirements and our duties.

Use of System Charges

Respondents' views

31. One respondent commented about a disparity between the definition of Distribution Use of System (DUoS) charges in the DCUSA and that in the distribution licence. The respondent highlighted its disappointment that this issue was not raised in Ofgem's notice of its intention to designate the DCUSA, but noted that the DCUSA (if designated) will provide a flexible governance regime which will enable industry to adapt and change the Agreement.

Ofgem's view

32. Ofgem notes the respondent's view that the DCUSA may provide a governance regime within which the issue it has identified can be addressed.

Notice period for varying DUoS Charges

Respondents' views

33. One respondent was concerned that the DCUSA does not reflect the requirement for a different notice period for notification of DUoS charges for embedded distribution networks. The respondent suggested that the DCUSA rather than the DUoS Charging Methodology was the correct place to reflect these different notice periods and would therefore suggested that the DCUSA be amended prior to designation.

Ofgem's view

34. Clause 19.1 requires DNOs and IDNOs to provide written notice to the User before varying charges. The notice period set out is 40 days, or such period specified in the Company's Relevant Charging Statement. Ofgem sees benefit in clearly defining the required notice period for varying DUoS charges in the DCUSA.
35. If Parties to the DCUSA consider that the current drafting is not adequate and requires further clarification, they are able to raise change proposals to the document in order to clarify terms.

Independent Distribution Network Operator (IDNO) – DNO relations

Respondents' views

36. Two parties suggested that further development of the DCUSA is still required, with the relationship between distributor parties where one distributor connects to another DNO or IDNO network being highlighted in particular. It was recommended that generic use of system and connection arrangements should be covered by the DCUSA, whilst site specific arrangements should be covered by a bilateral agreement. One respondent suggested that this would be consistent with the arrangements in place under CUSC for connections to the transmission system.
37. The respondents recognised the possibility for parties to raise change proposals to the DCUSA in order to address issues such as that described above. They also noted that the Panel is able to extend the timetable for the Assessment Process and expressed concern that any such extensions should not unduly delay the development of a solution to the 'network to network' issue.

Ofgem's view

38. We note that the industry has agreed that the development of sections of the DCUSA addressing the relationships between network operators is worthwhile. We also note that the timescale for developing the DCUSA was not conducive to the development of a wholly new section before designation, and that this may have been inconsistent with the task of converting the consolidated DUoS into the DCUSA.

39. Regarding the second concern, any decision to extend the timetable for assessment beyond the normal maximum prescribed within the DCUSA is subject to the oversight by the Authority. As in other industry documents, we will be keen to ensure that an expeditious and efficient development timetable is followed for all change proposals.

DCUSA preserving provisions from DUoSAs

Respondents' views

40. A concern was expressed that the Entire Agreement clause, clause 43.1, makes no reference to the arrangements proposed in the Termination Agreement. The respondent considered that without such a reference, it would not be possible to ensure the continuation of certain provisions set out or referenced in the DUoSA (preserved provisions).

Ofgem's views

41. Ofgem does not consider that this clause needs to refer to the Termination Agreement, in order to ensure that any preserved provisions can remain in force, as the clause does not have the effect of terminating previous agreements between parties.

Practical Issues

Respondents' views

42. One respondent was concerned that the DCUSA as currently drafted contained too many deficiencies and argued that designation should be postponed so that these issues could be addressed in a further draft. The respondent stressed that clarity as to the final terms of the DCUSA was essential before it could be acceded to by the company's board and called for this to be done before the document was designated by Ofgem.

Ofgem's view

43. Ofgem notes that the DCUSA is an evolving document and that while there are sections that may be less than perfect or subject to differences of opinion, parties have the ability to suggest improvements and for those proposals to be evaluated by their peers. Ofgem does not consider the issues outlined in this response to be significant enough to negate the overall benefit to be derived from designation of the DCUSA.

Overall Ofgem View

44. Ofgem acknowledges that there are outstanding issues related to the contents of the DCUSA. We note however that the DCUSA is an evolving document and parties have the ability to raise change proposals. A number of issues have been raised by respondents as potential areas for change. The change proposal mechanism enables them to ensure, should they wish, that the issues are considered at a later stage. For change proposals to part one, Ofgem will be required to determine whether a change proposal is made or not. Ofgem will consider any proposals in the context of prevailing conditions. It will take into account the views of respondents, the Applicable DCUSA Objectives and Ofgem's principal objective and

general duties when making its decision on a change proposal. Ofgem's future decisions on change proposals would not be fettered by any views expressed during the development of the DCUSA or in this letter.

45. It is our view that the DCUSA meets the requirements imposed upon it by Condition 9B. It is also our view that the benefits of designating the DCUSA outweigh the potential problems raised by respondents and that designation is in accordance with our principal objective and general duties set out in paragraphs 46-49 below.

Benefits of the DCUSA

46. Ofgem considers one of the major benefits of moving to the DCUSA arrangements, which was also recognised by many members of industry, will be the increase in the transparency of the arrangements. The document will be accessible to all participants and interested new participants on an agreed website. Changes to the document will be made via a transparent change process, within which all parties will have the opportunity to put forward their views. A single document will eliminate the potential for discriminatory treatment of parties by ensuring that the same basic terms apply to all counterparties. It will also allow for a consistent approach to be taken across distribution networks in Great Britain. Ofgem considers this increased transparency and consistency will lead to a promotion of competition within the sector.
47. We consider that designation of the DCUSA will promote efficiency and economy amongst electricity distributors and suppliers when carrying out their commercial operations in relation to connection to and use of the distribution networks. The multilateral arrangements will provide an established forum where commercial issues can be raised and resolved. It will allow issues applicable to a class of party across the sector to be resolved more efficiently. A single document should reduce the administrative burden upon participants as multiple bilateral changes will no longer be required. It can allow for cost savings through the existence of a well defined change process through which changes can be introduced wholesale, which allows for industry expertise and resource to be shared for the benefit of all market participants.
48. We consider that the DCUSA will be better placed to cope with future market developments and facilitate development of changes benefiting distributed generation across the distribution arrangements to a greater extent than would have been possible under the former bilateral arrangements.
49. The multilateral nature of the document will ensure that any such changes can be incorporated wholesale across the industry, rather than in a piecemeal fashion as would have occurred under the former arrangements. The transparent amendment process will provide an opportunity for industry knowledge to be shared allowing the potential for maximum benefit of such changes.

Direction of differences between consolidated DUoSA and DCUSA

50. Under the terms of Condition 9B the contents of the DCUSA at the date of designation must, save to the extent directed otherwise by the Authority, be the same as the text which comprises the consolidated DUoSA. Ofgem has reviewed the differences between the consolidated DUoSA and the DCUSA and has identified the occasions where there is a change and it is necessary to issue a direction. These are:

Standard Terms of Connection

51. The DCUSA differs in the manner in which contracts are established and maintained with customers. The relevant sections of the DCUSA include clause 17 and Schedules 2A and 2B. This change provides that the terms governing the relationship between distributors and customers will now be incorporated by reference. The reference will be to a website, where the terms will be listed and available to view by the customer or the terms can be requested by the customer to be sent to them by writing or by telephoning the Energy Networks Association. This change has been considered in detail by the DCUSA Steering Group and sub groups of the DCUSA Steering Group.
52. Ofgem considers altering the manner in which the legal relationship is established and maintained between distributor and customer to the method proposed in the DCUSA to be a positive development. It clearly defines the role of the supplier in procuring this relationship as agent, and once procured provides that the supplier need no more be involved. Ofgem considers that there are sufficient safeguards within this method to also protect the interests of customers. The existence of the terms and the fact that they will be binding when entering into a supply contract must clearly be brought to the attention of the customer by the supplier. Further, the terms sit in part one of the DCUSA and therefore can not be altered without the prior approval of the Authority.
53. Ofgem considers that it is in accordance with its principal objective and general duties to direct this change as the change creates a sufficiently transparent set of arrangements which will establish not only what terms the customer is contracting on but also with whom they are contracting.

Shared Market Domain IDs

54. We note that the DCUSA has been modified to enable more than one party to be associated with the same Market Domain ID. Ofgem notes the comments made by a respondent to the effect that these provisions may be inappropriate. We agree with this to the extent that the solution may undermine a basic, although important, concept. Whilst this is the case, we note that the impact of this provision is limited in terms of the circumstances where it can currently be practically applied, and that it is not possible for the situation which gave rise to the practical sharing of MDIDs to occur again in the future. We also consider that if approved this change would have minimal, if any negative impacts on market participants given that it is essentially an efficiency measure. As such we consider that the impact of this change is unlikely to be material.
55. In addition, to remove this addition to the DCUSA Ofgem would need to carry out a consultation on the amended text of the document for a further 28 days. We consider delaying the designation would run counter to our principal objective and general duties, given the benefits of the DCUSA. Therefore, we have decided that the most appropriate approach is for us make the direction. We note that parties to the DCUSA would be able to raise modifications to the document in order to more fully evaluate the impacts of a change.

Other Differences

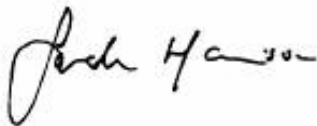
56. Ofgem notes that there are a number of other differences between the terms of the consolidated DUoSA and the DCUSA. Ofgem considers that some of these changes

have been made to provide greater clarity to the intent of the provisions that have been reproduced in the DCUSA. The remainder of these changes have been necessary because they are the consequence of moving from multiple bilateral arrangements to a multilateral set of arrangements. Ofgem considers using this opportunity to provide greater clarity will enhance transparency and lead to a more efficient set of arrangements.

57. For the reasons as set out above the Authority directed, on 29 September 2006, that the changes between the consolidated DUoSA and the DCUSA be made.

Conclusion

58. Having considered the responses received, Condition 9B and its principal objective and general duties, the Authority has today directed that the DCUSA submitted to the Authority on 29 August 2006, save as set out in the designation direction, be designated. The changes set out in the designation direction are not changes of substance, but flow from the designation of the DCUSA or add essential information that was not included in the draft submitted to Ofgem on 29 August 2006.



Sarah Harrison
Managing Director, Corporate Affairs
Signed on behalf of the Authority and authorised for that purpose